United States Court of Appeals

for the Second Circuit

PETITIONER'S REPLY BRIEF

77-4057

(Corrected Copy)

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

Nos. 77-4057, 77-4067,
77-4068, 77-4073,
77-4074, 77-4075

AMERICAN TELEPHONE AND TELEGRAPH COMPANY, ET AL.
Petitioners,
v.
FEDERAL COMMUNICATIONS COMMISSION AND
UNITED STATES OF AMERICA, Respondents,

MCI TELECOMMUNICATIONS CORP., ET AL., Intervenors.

On Petition for Review of Orders of the
Federal Communications Commission

Reply Brief of Petitioner American Telephone and Telegraph Company

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TABLE OF CONTENTS

Page

I. The Commission has violated unequivocal procedural requirements imposed by the controlling statutory provision..... 1

II. An evidentiary hearing was required to resolve numerous disputed issues of material fact..... 13

Conclusions..... 17

TABLE OF AUTHORITIES

Judicial Decisions:

AT&T v. FCC, 449 F.2d 439 (2d Cir. 1971)..... 2, 4, 5, 6, 7, 8, 16

AT&T v. FCC, 487 F.2d 865 (2d Cir. 1973)..... 3, 12

Bell Telephone Co. of Pennsylvania v. FCC, 503 F.2d 1250 (3d Cir. 1974), cert. denied, 422 U.S. 1026 (1975)..... 4

Independent Bankers Ass'n of Ga. v. Board of Govenors of F.R.S., 516 F.2d 1206 (D.C. Cir. 1975)..... 10

Mobil Oil Corp. v. FPC, 483 F.2d 1238 (D.C. Cir. 1973)..... 7

National Association of Motor Bus Owners v. FCC, 460 F.2d 561 (2d Cir. 1972)..... 4, 5, 6, 16

Public Service Commission v. FCC, 511 F.2d 338 (D.C. Cir. 1975)..... 16

United States v. Allegheny-Ludlum Steel, 406 U.S. 742 (1972)..... 11

United States v. Florida East Coast Ry., 410 U.S. 224 (1973)..... 9, 10, 11

United States v. Storer Broadcasting Co., 351 U.S. 192 (1956)..... 8

Washington Utilities & Transportation Commission v. FCC, 513 F.2d 1142 (9th Cir.), cert. denied, 423 U.S. 836 (1975)..... 4

WBEN, Inc. v. United States, 513 F.2d 1142 (7th Cir.), cert. denied, 393 U.S. 914 (1968)..... 8-9

TABLE OF AUTHORITIES CONTINUED

	Page
Statute:	
Communications Act, 47 U.S.C. § 205 et seq.....	Passim
Administrative Decisions:	
In re Telpak Sharing, 31 F.C.C.2d 674 (1971).....	5, 6
Matter of AT&T, 50 F.C.C.2d 501 (1974).....	8
Matter of AT&T, 62 F.C.C.2d 774 (1977).....	8

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I.

The Commission has violated unequivocal procedural requirements imposed by the controlling statutory provision

In ordering resale and sharing of private line communications services, the Commission has clearly prescribed both common carrier practices and rates within the meaning of Section 205(a) of the Communications Act, 47 U.S.C. § 205(a). The Commission itself has repeatedly conceded that its orders constitute

a prescription of carrier practices under Section 205(a).[1/] With respect to rates, this Court has previously emphasized that the inevitable result of sharing orders, such as the orders involved here, is a substantial and direct change of rates for numerous customers. AT&T v. FCC, 449 F.2d 439, 451 (2d Cir. 1971). The Court stated unequivocally that such orders "fix and prescribe rates . . . ." Id. While the Commission now asserts that this Court erred in that respect,[2/] it has also conceded that a "number of users" would in fact receive rate changes as a result of its orders here.[3/] In these circumstances, the Commission's prescription of the practice of resale and sharing plainly also involved a prescription of communications rates.[4/]

Unlike other sections of Title II of the Act that have sometimes been held to permit the use of abbreviated procedures, and in contrast to the summary procedures used here, Section 205(a) expressly requires that the Commission afford a "full opportunity

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1/ E.g., Commission's Memorandum in Opposition To Stay at 15; Respondent's Brief at 33, n.36; see also Brief of Intervenor IBM at 13.

2/ Respondent's Brief at 34, n.36.

3/ Report and Order at para. 49; 60 F.C.C.2d at 288; App. at 64-65.

4/ It should be observed that Section 205(a) is expressly applicable to prescriptions either of practices or of rates, so that, even if it were assumed that a prescription of rates might not be involved, the procedural and substantive requirements of Section 205(a) would nonetheless still be controlling here. The apparent reason for the Commission's efforts to deny that rate making has occurred is described below, at 7.

for hearing" before carrier rates and practices may be prescribed. (Emphasis added.) This unusual requirement reflects the special nature of the Commission's prescription power. The regulatory structure of the Act is premised upon the establishment by carriers of their practices and rates without prior approval of the Commission. AT&T v. FCC, 487 F.2d 865, 871 (2d Cir. 1973). While the Commission has authority to suspend or prohibit practices and rates in circumstances defined by the Act, such actions are taken in response to tariffs initially established by carriers.

When the Commission seeks to utilize Section 205(a) to prescribe rates and practices, it reverses the ordinary regulatory pattern, and undertakes functions that are normally performed only by carriers.[5/] In light of this reversal of the usual procedures, it is scarcely surprising that Congress has required the Commission to use Section 205(a) with extraordinary care, and only after full and reasoned exploration of the pertinent factual questions. The infrequently-used prescription remedy is surrounded with detailed substantive and procedural obligations, which the Commission must satisfy before it may compel carriers to adopt practices and rates which they have not initiated. In particular, Congress

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5/ Similarly, Section 214(d), which permits the Commission to prescribe various actions without carrier-initiation, including prescriptions of carrier routes, also requires a full hearing before the Commission may act. In contrast, when carriers seek Commission approval of carrier-initiated route proposals under other provisions of the Act that do not require a full hearing, summary

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understandably emphasized the importance of thorough consideration of factual matters by insisting that the Commission conduct "full" hearings before it prescribed practices or rates.[6/]

Both this Court and the Commission[7/] have previously held that informal "notice and comment" procedures, such as those used here, are inadequate and that a full evidentiary record is essential to resolve disputed issues of fact before rates and practices may be lawfully prescribed under Section 205(a). Contrary to the Commission's claim,[8/] National Association of Motor Bus Owners v. FCC, 460 F.2d 561 (2d Cir. 1972), plainly shows that both this Court and the Commission have previously recognized the full procedural requirements of the statute. NAMBO grew out of an earlier Commission effort to prescribe unlimited sharing of Telpak, a private line service offered by AT&T. The Commission's present orders are intended to achieve

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procedures have been held to be acceptable. See, e.g., Washington Utilities & Transportation Commission v. FCC, 513 F.2d 1142 (9th Cir.), cert. denied, 423 U.S. 836 (1975). See also Bell Telephone Co. of Pennsylvania v. FCC, 503 F.2d 1250 (3rd Cir. 1974), cert. denied, 422 U.S. 1026 (1975).

6/ Congress also expressly required that specific findings be made before a prescription may be ordered. As shown in AT&T's principal brief at 39-42, the Commission failed to make reasoned or adequate findings here. See also AT&T v. FCC, supra, 449 F.2d at 450-52.

7/ Prior decisions of the Commission which acknowledged the need for evidentiary hearings before prescriptions may be made under Section 205(a) are listed in AT&T's principal brief at 23.

8/ Respondent's Brief at 38-39; see also Brief of Intervenor IBM at 24-27; Brief of Intervenor CBEMA at 15.

precisely the same result.[9/] The Commission's first effort was found unlawful because it failed both to make the findings required by Section 205(a) and to conduct evidentiary hearings to resolve disputed factual issues before prescribing carrier rates and practices. AT&T v. FCC, supra, 449 F.2d 439.[10/] Nonetheless, the Commission has again utilized the same shortcuts here in an effort to achieve exactly the same goal.

On remand from this Court in 1971, the Commission expressly recognized that under the Court's Telpak sharing decision a prescription would require "further proceedings" to develop a "fuller evidentiary record." In re Telpak Sharing, 31 F.C.C. 674, 675 (1971). In light of that requirement, the Commission decided not to utilize its prescription authority under Section 205(a). In affirming the Commission's decision not to employ its prescription authority, this Court stated in NAMBO that the agency had accurately construed the Court's mandate in AT&T v. FCC, supra, to require prescription orders to be based on a full

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9/ The Commission has made clear that one of the principal services that would be subject to its orders here is again Telpak. (Report and Order at para. 49; 60 F.C.C.2d at 288; App. at 64-65.) The orders involved here are indistinguishable from the Commission's earlier Telpak sharing order, which was set aside by this Court because of the Commission's failure to comply with Section 205(a), except that the Commission has swept up in its orders here various private line services in addition to Telpak.

10/ See also National Ass'n of Motor Bus Owners v. FCC, supra, 460 F.2d at 563, where this Court, in discussing the requirements of Section 205(a), said that in the first Telpak sharing case "no such hearing had been held nor had findings been made." (Footnote omitted.) If the Commission's present claims were correct, the absence of such an evidentiary hearing would of course have been entirely immaterial.

evidentiary record. 460 F.2d at 564. The Court noted that the Commission had properly recognized the "necessity of holding evidentiary hearings" before a final prescription order could be entered pursuant to Section 205(a). Id. In short, NAMBO shows unequivocally that both this Court and the Commission construed Section 205(a) to require the Commission to conduct evidentiary hearings before it may prescribe practices or rates under Section 205(a). Such a construction is irreconcilable with the procedural shortcuts that were adopted by the Commission here, precisely as it was with the use of the same shortcuts in the Commission's first Telpak order.

Here, reversing its own holding in Telpak Sharing, the Commission now claims that the full hearing requirement of Section 205(a) may after all be satisfied merely by the use of informal rulemaking devices -- in this case, "notice and comment" procedures. The Commission asserts that its collection of informal and unverified comments is sufficient, without the conduct of an evidentiary hearing, to resolve the numerous and substantial factual questions that AT&T has shown to exist concerning the impact and desirability of private line resale and sharing. In substance, the Commission asserts that it can obliterate the recognized differences between informal rulemaking and rate making, and repeal by its own order the procedural obligations imposed by Congress upon the Commission's exercise of its special prescription authority under Section 205(a).

The Commission's claims are dependent, not only upon a nullification of Section 205(a), but also upon the abandonment of well-settled principles for the conduct of rate making proceedings. As described above, the Commission has, despite a contrary ruling by this Court, AT&T v. FCC, supra, 449 F.2d at 451, claimed that its prescription of the practice of resale and sharing does not involve a prescription of rates. The reason for the Commission's strenuous efforts to overturn this Court's decision may readily be inferred. The Commission evidently hopes to circumvent the well-settled principle that rate making, although sometimes described as a form of rulemaking, nonetheless requires "an adjudicative resolution of disputed facts." Mobil Oil Corp. v. FPC, 483 F.2d 1238, 1257 (D.C. Cir. 1973).

In accordance with the special requirements of rate making proceedings, the Commission itself has, without exception, conducted evidentiary hearings to investigate carrier revenues, establish carrier rates of return, and resolve questions of the lawfulness of individual rates.[11/] Even where it has adopted procedural expedients to simplify and expedite such hearings, it has preserved the right of cross-examination and taken care

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11/ Indeed, AT&T is unaware of any case since the initiation of interstate regulation in 1887 with the Interstate Commerce Commission where informal "notice and comment" procedures analogous to those used here were utilized by any federal regulatory agency to prescribe common carrier rates.

that matters of disputed fact would be adequately investigated.[12] Here, as with the Commission's first Telpak sharing order, the mere fact that rate making is prospective cannot eliminate the requirement that a full evidentiary record must be developed before rates may be established or altered. AT&T v. FCC, supra, 449 F.2d at 451. Without an evidentiary hearing to permit an adjudicative resolution of disputed factual issues, the Commission's latest resale and sharing order, like its previous Telpak sharing order, is fatally defective.[13]

12/ Thus, the Commission has experimented in the use of "paper" hearings, in which the use of written testimony, interrogatories and information requests is encouraged in lieu of full oral presentations of evidence. E.g., Matter of AT&T, 50 F.C.C.2d 501, 515 (1974). Nonetheless, it has carefully emphasized in such cases that oral testimony will be permitted to preserve rights of cross-examination and where written submissions would not provide satisfactory opportunities to develop evidence. Id. at 516. See also Matter of AT&T, 62 F.C.C.2d 774, 776, n.4 (1977). Such "paper" hearings have involved a mixture of oral and written testimony designed to expedite the resolution of issues and to minimize costs. In contrast, the informal "notice and comment" procedures used here did not offer any opportunity for cross-examination or permit the development of a meaningful evidentiary record. The informal procedures used here have never, so far as AT&T is aware, been used for the prescription of rates, and afforded none of the protections which have been carefully preserved in the Commission's experiments with "paper" hearings. Far from supporting the procedures here, those experiments show vividly the novelty and inadequacy of what the Commission has done.

13/ Because United States v. Storer Broadcasting Co., 351 U.S. 192 (1956), and WBEN, Inc. v. United States, 513 F.2d

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Nor are the Commission's claims supported by the principal case upon which it has relied, United States v. Florida East Coast Ry., 410 U.S. 224 (1973).[14] To be sure, the Supreme Court in Florida East Coast concluded that the use of the word "hearing" alone in Section 1(14)(a) of the Interstate Commerce Act was insufficient to require the conduct of an evidentiary hearing.[15] In contrast, however, Section 205(a) of the Communications Act expressly requires a

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1142 (7th Cir.), cert. denied, 393 U.S. 914 (1968), did not involve rate making and also did not involve the special structure established by Congress in Title II of the Act, they provide no support for the use of informal rulemaking procedures where, as here, the Commission's authority under Section 205(a) is employed to prescribe carrier practices and rates. See also AT&T's principal brief at 28, n.33.

14/ The Commission, in relying in its brief exclusively on Florida East Coast, apparently has abandoned various other arguments it offered in its prescription orders for utilizing only "notice and comment" rulemaking procedures. (Report and Order at Appendix D; 60 F.C.C.2d at 325-30; App. at 117-26.) In addition to Florida East Coast, the Commission there relied on the asserted presence of general policy questions common to a large number of regulatees; Sections 4(i) and 4(j) of the Communications Act; and the legislative history of the Communications Act with respect to the hearing provisions under Title II. AT&T showed in its principal brief (at 19-21, 24-37) that none of those arguments, including the Commission's reliance on Florida East Coast, supports the use of informal rulemaking procedures here. As to all but its reliance on Florida East Coast, the Commission's silence evidently indicates its agreement with AT&T's analysis.

15/ Respondent's Brief at 34.

"full opportunity for hearing" before rates or practices may be prescribed. (Emphasis added.) Moreover, the Supreme Court made clear that its decision in Florida East Coast depended heavily on the special functions and particular legislative history of the statute before it.[16/] It indicated that the absence of the words "on the record" in Section 1(14)(a) was dispositive of the form of hearing required there chiefly because that statute had been comprehensively reviewed and then amended by Congress in 1966. Id. at 231. This occurred long after the enactment of the Administrative Procedure Act, in which the so-called triggering words "on the record" were included. In contrast, Section 205(a) of the Communications Act was enacted in 1934, more than a decade before the Administrative Procedure Act, and has not since been amended. In these circumstances, no significance can be retrospectively attributed to Congress' omission of the words "on the record" in the description of the type of hearing required by Section 205(a).

Moreover, Section 205(a) was clearly intended to require the Commission to exercise its unusual prescription remedy only after thorough and careful examination of relevant factual issues. In contrast, the statute

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16/ Florida East Coast has been distinguished by another Circuit precisely on the basis of the unusual character and background of the statute involved there. Independent Bankers Ass'n of Ga. v. Board of Governors of F.R.S., 516 F.2d 1206, 1218 (D.C. Cir. 1975). See also AT&T's principal brief at 19-21, 36 n. 45.

construed by the Supreme Court in Florida East Coast was motivated by a special need for urgent governmental action. Section 1(14)(a) was originally enacted to enable the Interstate Commerce Commission to remedy specific problems that arose from a particular crisis -- a wartime shortage of railway freight cars.[17/] The statute was amended in 1966 to give the Interstate Commerce Commission even more effective authority to deal expeditiously with a continuing railway car shortage that had reached dangerous proportions. Id. at 231. In fact, after the Interstate Commerce Commission delayed using its new authority, congressional hearings were held at which the ICC was warned that immediate action was expected. Id. at 232. Yet, even after this unequivocal expression of Congress' expectation that it should act quickly to remedy an urgent problem, the ICC, unlike the Commission here, still provided a meaningful opportunity for interested parties to develop an evidentiary record concerning disputed facts. In this instance, the Commission has not and cannot point to any legislative history to justify its use of the summary and informal procedures employed here. If anything, Florida East Coast shows vividly the absence of any possible justification for the Commission's disregard of the procedural requirements of Section 205(a).

17/ United States v. Allegheny-Ludlum Steel, 406 U.S. 742, 744 (1972).

The statutory requirements applicable here cannot be abolished by administrative order even if, as the Commission now intimates, some degree of delay might result if the statute were obeyed.[18] If obedience to Section 205(a) requires a more careful examination of disputed factual issues than the Commission prefers to undertake, it may seek suitable relief from Congress. Even if it were true that the Commission's shortcuts here represent an "enlightened" and "modern" approach,[19] only Congress -- and not the Commission -- has authority to change Section 205(a) to permit such an approach. As this Court has already emphasized, the Commission may not alter the statutory accommodation of conflicting interests and values that was established by the Congress in Section 205(a):

> "In balancing the various interests involved, Congress provided the comprehensive statutory plan [of Sections 205-205 of the Act]. The Commission is not authorized to circumvent this statutory scheme by making its own equitable adjustments." AT&T v. FCC, supra, 487 F.2d at 881.

18/ Respondent's Brief at 30. In fact, however, the Commission never claimed in the orders under review here that adherence to the procedural requirements of Section 205(a) was impractical. To the contrary, the Commission's original Notice appeared to contemplate the procedures demanded by the section, and the Commission only belatedly elected to utilize the shortcuts at issue here. Moreover, this proceeding required only approximately two years between the original Notice and final orders, which can scarcely be regarded as too slow given the complexity of the issues and the length of other Commission proceedings. Any claim of impracticality now would merely represent counsel's rationalization for actions taken on the basis of entirely different grounds. See also AT&T's principal brief at 39, n.47.

19/ Brief of Intervenor CBEMA at 13.

The Commission's failure to comply with the procedural requirements imposed by Congress clearly requires that its orders be set aside.

II.

An evidentiary hearing was required to resolve numerous disputed issues of material fact

The Commission has suggested that AT&T only disagrees with the Commission's procedural determinations, and that it does not contest the "reasonableness" of the practices and rates that the Commission has prescribed.[20/] AT&T certainly believes that the Commission has disregarded important statutory obligations that require its orders to be set aside, but it completely misconstrues AT&T's position to claim that it does not also dispute both the "reasonableness" of the Commission's orders and the factual assumptions upon which those orders are based. To the contrary, AT&T has strongly urged that the Commission has adopted novel and far-reaching requirements without a rational evaluation of their consequences. Moreover, in so doing the Commission has arbitrarily rejected the only specific factual analysis before it of the adverse implications of resale and sharing.[21/]

The basic question in this proceeding is whether, and under what conditions, subscribers should be allowed to resell communications services to others or to participate with others in the sharing or joint use of such services. In purporting to find sharing and resale to be in the public interest, the

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20/ Respondent's Brief at 25.

21/ See, e.g., AT&T's principal brief at 15, 42-48.

Commission necessarily rejected AT&T's contention that only limited and specific changes in existing tariff restrictions should be ordered. In so doing, the Commission also necessarily resolved numerous factual issues that were disputed by AT&T and other parties. All of those disputed factual matters clearly required the conduct of an evidentiary hearing under Section 205(a) before the Commission could make a rational appraisal of the far-reaching implications of its orders.

For example, the Commission rejected AT&T's contention that private line resellers would not enable the public to manage their communications networks more efficiently. The Commission reached this conclusion merely upon the basis of its belief, which was not supported by any facts contained in the record, that resellers will have potentially greater interests in and capabilities for communications network management than existing carriers.[22/] Similarly, when AT&T urged that the creation of layers of intermediaries would seriously hinder accurate forecasts of future service needs and demands, the Commission did not pause to explore that factual question through an evidentiary hearing. Instead, it simply disregarded AT&T's contention and asserted that the creation of middlemen would in fact facilitate such forecasting.[23/] Throughout the Commission's discussion of the supposed benefits and lack of disadvantages of resale and

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22/ Report and Order at para. 77; 60 F.C.C.2d at 299; App. at 79.

23/ Report and Order at para. 80; 60 F.C.C.2d at 300; App. at 80.

sharing, it sought in the same way to resolve important factual issues merely by assuming or believing or expecting them away.[24/]

The Commission's failure to conduct an adequate factual inquiry is particularly blatant with respect to the revenue and rate impact of resale and sharing. It is indisputable that AT&T and the Commission are in sharp disagreement as to the nature and significance of that impact, and that any meaningful consideration of such questions must necessarily involve a resolution of important factual matters. Accordingly, there should presumably also be no dispute that Section 205(a) requires an evidentiary hearing at least with respect to those factual matters. Nonetheless, the Commission has unaccountably claimed that revenue and rate questions do not "lend" themselves to evidentiary resolution,[25/] ignoring the fact that it has since its creation conducted evidentiary hearings to investigate carrier rates which will obtain in the future and which are based on forecasts of future events.[26/] Moreover, the Commission's claim is inconsistent with this Court's determination that factual questions of rate and revenue impact are entirely susceptible to resolution through the very procedures which the Commission has sought here

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24/ Report and Order at paras. 75-88; 60 F.C.C.2d at 298-303; App. at 78-83. The Commission's analyses of these points, as well as those discussed in the following paragraph, fell far short of that required for reasoned decisionmaking in any context, and certainly do not satisfy the special requirements imposed by Section 205(a).

25/ Respondent's Brief at 41.

26/ Supra, at notes 11 and 12.

to avoid.[27/] The Commission's refusal to conduct evidentiary hearings in which such disputed factual issues could be rationally resolved meant that it could not "give reasoned consideration to the ultimate issue presented -- the balancing between the costs and benefits." Public Service Commission v. FCC, 511 F.2d 338, 349 (D.C. Cir. 1975).

While recognizing the far-reaching implications of its prescription of resale and sharing, the Commission has sought to justify its restructuring of the communications industry merely upon the basis of its "reasonable expectations" as to essential aspects of its orders.[28/] Each of those "expectations" was founded on numerous assumptions, rather than supported findings of fact, regarding such matters as the range and scope of user needs; whether present carriers are able to satisfy those needs; and the impact of resale and sharing on AT&T's resources, AT&T's traffic, AT&T's rates and AT&T's revenues.[29/] Although AT&T disputed virtually all of the factual assumptions made by the Commission in deciding those issues, the Commission nonetheless declined to hold hearings in which an adequate evidentiary record could have been developed to resolve the disputes. The

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27/ AT&T v. FCC, supra, 449 F.2d 439; National Ass'n of Motor Bus Owners v. FCC, supra, 460 F.2d at 564.

28/ Report and Order at para. 88; 60 F.C.C.2d at 303; App. at 83.

29/ Report and Order at Appendix B; 60 F.C.C.2d at 322; App. at 111-13.

Commission was instead content to act merely upon the basis of its own "theorems" without, as Commissioner Hooks candidly recognized, even "a scintilla of economic data" to support or justify them.[30/] The Commission's failure to make a rational appraisal of the far-reaching consequences of its orders requires that those orders be set aside.

Conclusions

For reasons stated above and in AT&T's principal brief, the orders under review should be set aside and enjoined. For reasons stated in AT&T's principal brief, a stay pendente lite should be entered to prevent the effectiveness of the orders pending the completion of judicial review.

Respectfully submitted,

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30/ 60 F.C.C.2d at 337; App. at 142.

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Re: AT&T, et al., v. FCC, et al.,
Nos. 77-4057, 77-4067, 77-4068,
77-4073, 77-4074, 77-4075

Dear Sir:

Since the filing of the Reply Brief of American Telephone and Telegraph Company in the above titled cases, we have discovered a typographical error on page 10. I have enclosed ten copies of the Reply Brief with the error on that page corrected. Apart from the correction, no other change has been made in the Reply Brief. I request that the enclosed ten copies be substituted for those previously filed with the Court. Copies of the corrected page have been provided to all counsel.

If there are any questions regarding this matter, please telephone me collect at the number shown above.

Very truly yours,

Charles Lister

CL/s
Enclosures